Iowa Finance Authority

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Credit Profile

OUTLOOK REVISED	**To**	**From**
Iowa Fin Auth ICR	AA-	AA-
OUTLOOK:	POSITIVE	

Rationale

Standard & Poor's Ratings Services revised its outlook to positive from stable and affirmed its 'AA-' issuer credit rating (ICR) on Iowa Finance Authority (IFA). The rating is based on the following strengths:

- The very high quality and very low-risk profile of the authority's asset base;
- Stable financial performance;
- High debt rating (around 97% rated 'AAA'), and minimal GO debt exposure;
- Strong and active management team that has a positive relationship with state government; and
- Rebounding state economy.

IFA is close to completing its five-year strategic plan adopted in 2003. The plan primarily focused on increasing the authority's asset base to 140% of fiscal 2003 levels while maintaining a stable financial performance. Four years into the plan, the authority has already achieved this goal without taking on any increased risk to its asset portfolio, which primarily comprises high credit quality Ginnie Mae and Fannie Mae MBS under the single-family program and minimal issuance under the multifamily program. The strength of the asset portfolio is complemented by good profitability ratios given the portfolio composition and the authority's sound equity position (more than 16% of total assets at the end of fiscal 2006). The decline in equity ratios over the past few years was expected as IFA rapidly expanded its asset base, but now that it has achieved its growth goals, equity ratios are expected to level off as IFA changes its course over the next few years, with a new strategic plan expected in fiscal 2007. IFA has a strong management team that has repeatedly proven to be proactive and successful in meeting its mission of financing affordable housing for residents of the state of Iowa. In addition, the management team has a positive and mutually beneficial working relationship with the state legislature.

The authority also administers, in partnership with the Iowa Department of Natural Resources, the State Revolving Fund (SRF), which issues tax-exempt bonds to finance wastewater and drinking water facilities. The SRF bonds are rated 'AAA' based on the large size and diversity of the SRF program's loan portfolios, program coverage and reserve levels, structural features, and a management team with a proven track record. Standard & Poor's analysis of the authority's ICR excludes the activities of SRF, as its funds are legally obligated to the program and hence do not contribute to IFA's finances.

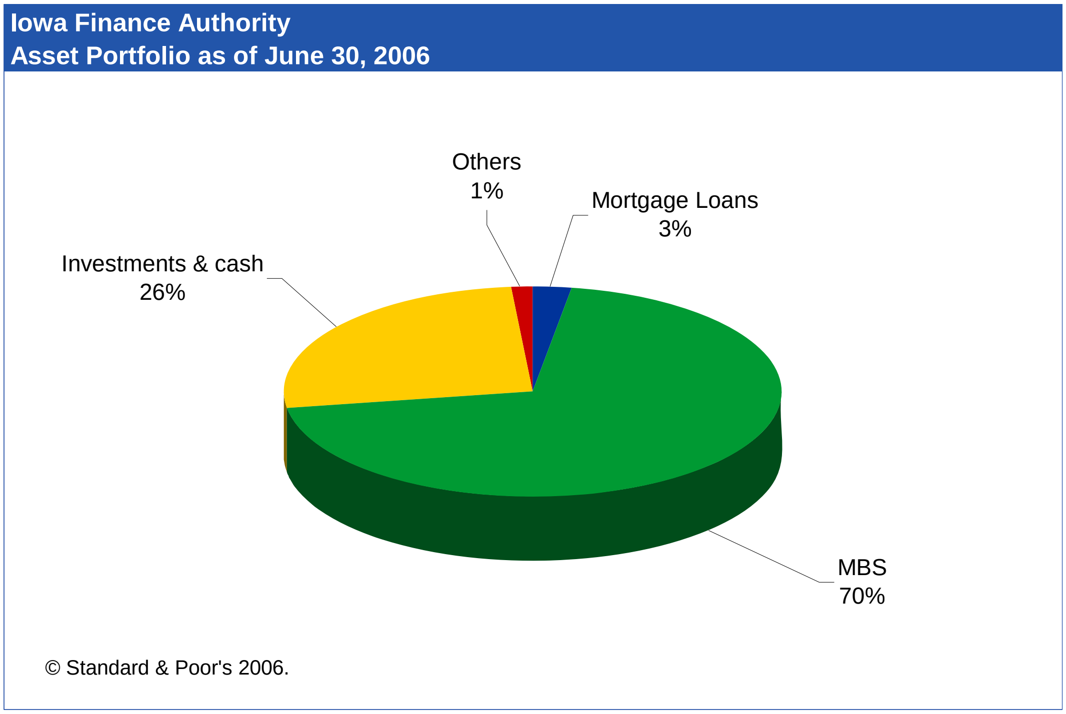
IFA's title guaranty division (TGD) was established in 1985 to guarantee title to real property in Iowa. The TGD is considered when evaluating IFA's ICR, as surplus funds from TGD, in accordance with state code, are available to support IFA's affordable housing activities. In fiscal 2006, TGD transferred $1.8 million to IFA's housing assistance program funds. The risk associated with title guaranty to IFA's ICR is viewed as minimal, as adequate reserves and reinsurance are in place to cover potential claims.

Outlook

The positive outlook reflects the strength of the authority's asset base, stable financial performance, and superior management, particularly during the authority's aggressive five-year strategic plan. Should the authority's financial performance continue, with improving trends and a leveling off of leverage ratios, the authority will be a candidate for a raised rating. However, if assets endure unforecasted growth, leading to a weakening of leverage ratios, the authority's 'AA-' ICR may be affirmed.

Asset Quality

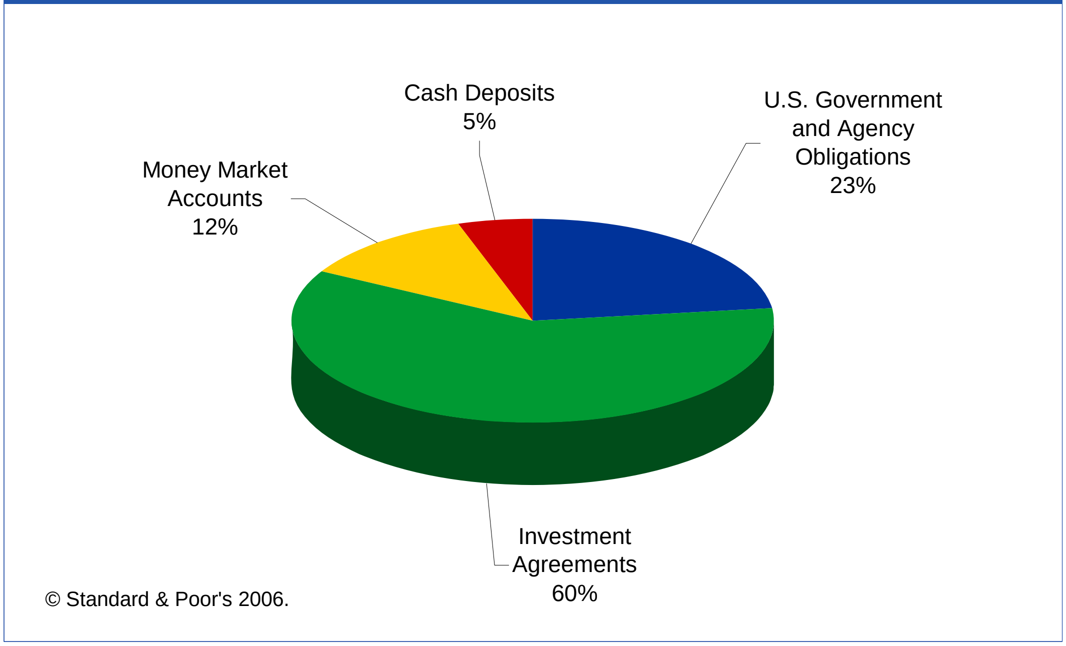
IFA's asset base has more than doubled in size since the beginning of fiscal 2000, again, largely due to the authority's strategic plan to expand its asset base and increase profitability. In fiscal 2006 alone, its asset base grew by about 26%, reaching an all-time high of approximately $950 million at the end of the fiscal year. Around 73% of its asset portfolio consisted of single-family MBS and other mortgage loans, and 27% represented high-quality investment securities and cash. The proportion of MBS and other mortgage loans in the asset portfolio rose from 48% of total assets since 2000, primarily due to increased lending activities. IFA's single-family MBS portfolio has more than quadrupled in size since 2000 and increased by a substantial 32% since 2005 alone, due to an increase in loan originations and thus the amount of MBS purchased. At the end of fiscal 2006, IFA's loan portfolio consisted of single-family Ginnie Mae and Fannie Mae MBS (97%) and single-family whole loans and multi-family loans (3%). In June 2006, the authority purchased land and buildings financed by a line of credit of $2.6 million to serve as the authority's operating location after its then-current lease expired.



IFA's loan portfolio is extremely low risk due to the authority's conservative approach to collateral. As of June 30, 2006, Ginnie Mae and Fannie Mae MBS backed more than 99% of IFA's single-family loans. As expected, delinquencies and non-performing assets as of June 30, 2006 were negligible, given the low risk associated with IFA's loans. Since MBS guarantee payment on the underlying loans, no reserves are required. However, for the remaining loans, IFA provides sufficient reserves to cover potential credit losses on the portfolio. These loans are performing well and have sufficient excess assets that cover any credit shortfall or liquidity issues.

IFA's investments as of June 30, 2006 were of high credit quality and provided ample liquidity, primarily consisting of investments in government securities and investment agreements rated 'AA-' or higher. Management takes a conservative approach to the oversight and monitoring of the authority's investments. Furthermore, IFA's investments continued to provide around 16% of total revenues in 2006. IFA's investments are extremely liquid, with approximately 90% of them maturing in less than a year.

Iowa Finance Authority
Investment Portfolio as of June 30, 2006



Earnings Quality And Financial Strength

Total revenues have increased steadily and have almost doubled in size since 2000. In 2006, revenues from IFA's core business of financing below-market rate, single-family mortgages increased by around 23% from 2005, due in part to increased marketing of IFA's products and rising interest rates. Net income continued to grow, however, it was impacted by higher operating expenses, and increasing interest expenses for bonds as IFA has implemented its strategic plan for growth. In addition, there have been fluctuations in the figures of grants received and disbursed over the past few years, particularly in 2005. IFA received a non-recurring state appropriation in 2005 that caused net income to be notably high, resulting in net income of $8.5 million in 2006, down 12% from the 2005 figure. If we were to exclude the 2005 appropriation, IFA's net income would reveal an increasing trend since 2004. IFA also administers the private activity volume cap allocated to certain private activity bonds, and therefore acts as a conduit bond issuer for various types of financing within the state, but does not report this function in its financial statements. These activities enable the authority to earn fee-based revenue without adding to its risk profile as a housing agency.

IFA's profitability, as measured by return on assets, declined to 1.00% in 2006 from 1.35% in 2005. Again, the decline is mainly attributable to an increase in receipts received from state appropriations in 2005, a significant proportion of which is held in revolving loan funds. Furthermore, its net interest margin (NIM) remained stable at 1.22% in 2006. Though the authority's NIM is lower than in previous years, it is not an area of concern given the limited risk profile of the authority's existing asset base. As detailed in table 2, the five-year average of the authority's profitability ratios is higher than those of its 'AA-' rated peers, exhibiting its strong financial performance.

IFA's equity position has increased by approximately 7% over the past year to $156 million in 2006, representing 16.41% of total assets. Unlike other housing finance agencies (HFAs), this ratio has declined steadily from 26.61% in 2000 as a result of the rapid increase in assets in accordance with the authority's strategic plan. The authority's equity base is adequate, however, to support its low-risk profile, and reflects the authority's significant financial strength. After adjusting for potential losses, the authority's unrestricted equity as a percentage of debt far exceeds Standard & Poor's threshold of 4% and its liquid assets are also well in excess of 2% of mortgage loans outstanding. IFA's sound capital adequacy ratios continue to indicate good management and a prudent use of authority resources.

Debt

As of June 30, 2006, IFA's debt outstanding totaled $765.58 million, up 31% from the preceding year and the highest level since the 1990s. The issuance of single-family bonds to finance the purchase of MBS under the authority's FirstHome Program accounts for the increase in debt. Of the total, around 97% are single-family bonds, with the remainder in multifamily bonds. All single-family bonds issued since 1991 under the single-family MBS resolution, constituting more than 99% of the total single-family bonds and around 97% of total debt, are rated 'AAA', reflecting the extremely high quality of pledged collateral, consisting of Ginnie Mae and Fannie Mae MBS, the strong credit quality of investments, and cash-flow sufficiency. The remaining single-family bonds backed by single-family whole loans and the multifamily bonds (series 1978A) are both rated 'AA' based on the strength of the excesses under the separate indentures. Under the series 1978A bond issue, loans are no longer outstanding and the bonds are solely secured by government obligations escrowed through bond maturity in 2021. Although IFA's GO is pledged to two out of the three parity resolutions outstanding, 97% of the bonds are held under the single-family MBS resolution, and therefore pose minimal risk to the authority's ICR. The authority's GO debt exposure ratio is 3.2%, ranking "low" on Standard & Poor's leverage scale for state HFAs.

In September 2006, the authority issued $6.8 million in multifamily bonds secured by its general obligation. The potential loss on these multifamily loans would need to be supported by the authority's general obligation and had a minimal impact on the authority's capital adequacy. Issuance of additional bonds under this new multifamily resolution ultimately increases the risk associated with the authority's assets but at this point, the impact is minimal given the size of the issue. Standard & Poor's will continue to track potential losses to the authority's capital as additional issuances occur.

At the end of June 2006, more than 26% of the single-family bonds outstanding were issued at variable interest rates. The use of variable-rate debt facilitated a reduction in the authority's cost of debt and origination of mortgage loans at competitive interest rates. Over the years, the authority hedged about 90% of its floating-rate exposure through interest rate swaps and caps entered into with either UBS AG ('AA+/A-1+') or Goldman Sachs Capital Markets LP (with a Goldman Sachs Group guarantee; 'AA-'). Following a review of IFA's 10 interest rate swaps and two interest rate caps, Standard & Poor's assigned the authority a Debt Derivative Profile (DDP) score of '2' on a four-point scale, where '1' represents the lowest risk and '4' the highest risk.

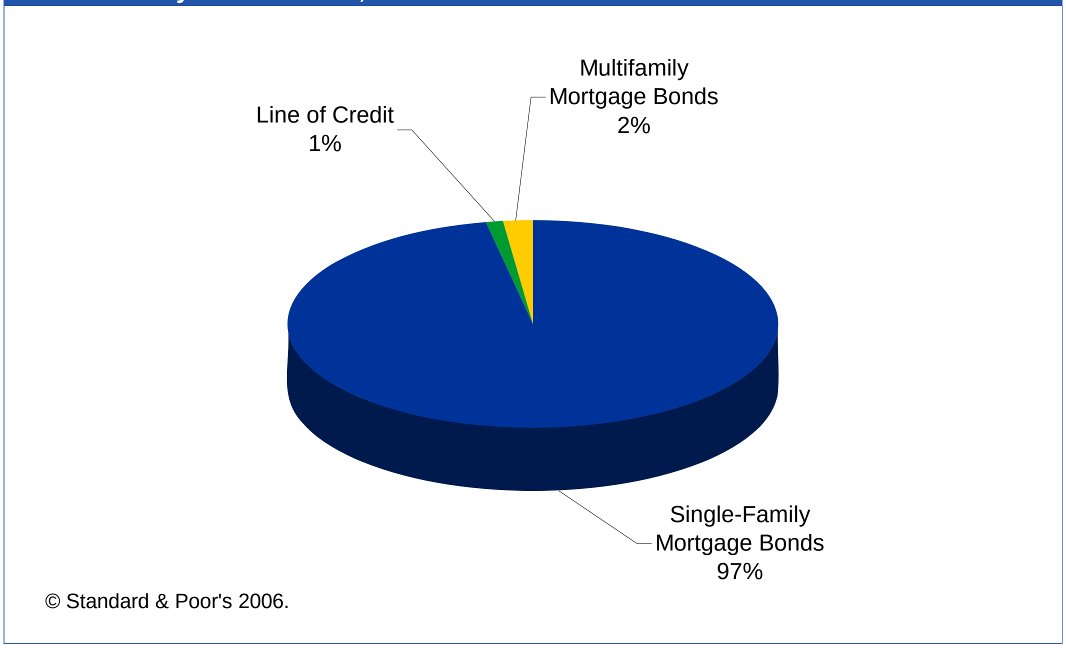
The overall score of '2' reflects:

- Two highly rated swap counterparties, both of which are required to post collateral before a credit event occurs;
- Moderate economic viability of the swaps due to the hedge rate being about 68% of LIBOR;
- Low termination risk; and
- Good management oversight.

Management is proactive in monitoring risks and benefits associated with swaps. It also ensures that the authority's exposure to either of its counterparties does not exceed a defined amount.

Standard & Poor's is not factoring in the value at risk as a contingent liability at this time due to the remoteness of involuntary termination.

Iowa Finance Authority
Debt Summary as of June 30, 2006



Management

The primary goal of the authority's five-year strategic plan implemented in fiscal 2003 was to increase the scope of its mission to provide affordable housing within the state. The plan called for rapid growth by increasing the size of its single-family program; implementing a new multifamily program that would add $40 million in new production; increasing profitability while expanding the size of the authority; and developing other sources of revenue that would keep IFA on track with its mission. Four years into the plan, IFA has already realized its goal of increasing its asset base to 140% of fiscal 2003 levels. Over the past few years, the authority increased single-family originations through a combination of efforts that included improved marketing and streamlining its loan origination and closing process. IFA successfully balanced its rapid growth while maintaining financial ratios, reflecting the strength of its active management.

The authority is governed by a nine-member board, appointed by the governor with the approval of two-thirds of the members of the state senate. An experienced professional staff backs the board with more than 80 employees, headed by an executive director who assumed office in 2005. The executive director had served as the chief financial officer of the authority since 2003, and was involved in the initial implementation of the authority's strategic plan. The succeeding chief financial officer had served as general counsel for the authority since 2001 before being appointed to his new position. Senior management has an average tenure of six years. IFA's strong and capable management actively seeks to improve financial performance and programmatic operations.

Standard & Poor's views IFA's relationship with the state as highly positive and expects this relationship to continue. IFA's legislative liaison coordinates meetings with legislative staff members to increase awareness of IFA and its programs, which thus far enabled IFA to garner support when needed. In fiscal 2005, IFA worked with the Iowa National Guard to introduce a veterans' down-payment assistance program that has become very successful and popular among legislators, who appropriated $2 million to the program in fiscal 2006 compared to $1.05 million in fiscal 2005. Additional appropriations are expected going forward. The authority also received appropriations for various programs run by IFA: Transitional Housing for Substance Abuse, Entrepreneurs with Disabilities Program, and the Home and Community Based Rent Subsidy Program.

The state continues to engage IFA to take on non-housing related activities, including serving as one of the state's primary bond issuing authorities. IFA's close relationship with the state is also evident through its role as administrator for the SRF, in partnership with the Iowa Department of Natural Resources, and its role as the state's allocating agency for low-income tax credits. In addition to its active single-family program, IFA manages a number of housing development and rehabilitation programs designed to provide affordable housing and improve existing housing stock. IFA also administers federal programs, including serving as contract administrator for Section 8 properties, Affordable Assisted Living Program, and the Low-Income Housing Tax Credit Program (LIHTC), thus strengthening its legislative mandate.

Economy

Iowa's diverse economy began to pick up steam in 2004, after a slow-growth period from 2001-2003. The state economy is grounded in the services, manufacturing, and agriculture sectors. Historically, a tight labor market has hampered Iowa's economy, due to a dwindling number of young people living in small towns and on farms available to take services and manufacturing jobs in the cities and a limited number of people moving to the state. This situation has eased somewhat in recent years with the increase in the state's jobless rate. Though the state's unemployment rate climbed to 4.1% in January 2006, it was still below the national average of 4.7%. Meanwhile, according to the U.S. Department of Labor's Bureau of Labor Statistics, the number of people employed in the state rose to 1.60 million in January 2006 from 1.55 million in 2003. Employment in Iowa is expected to grow 1.8% in 2006. According to the Bureau of Economic Analysis, Iowa's personal income growth rate of 4.9% is trailing the national average of 5.5%.

Iowa's housing activity continued to surge throughout 2005. Total housing starts for January 2006 were at 18,000 units combined for single- and multi-family housing units, a 33.3% year-on-year increase.

Table 1

Iowa Finance Authority Financial Ratio Analysis

	2002	***2003***	***2004***	***2005***	***2006***	***5-year average***
Profitability (%)						
Return on average assets	1.42	0.95	0.68	1.35	1.00	1.08
Return on assets before loan loss provision and extraordinary item	1.34	1.00	0.67	1.45	0.97	1.09
Net interest margin	1.50	1.20	0.98	1.22	1.22	1.22
Asset Quality (%)						
NPAs/total loans and real estate owned	0.00	0.00	0.05	0.08	0.10	0.05
Loan loss reserves/total loans and MBS	0.00	0.75	0.45	0.42	0.33	0.39
Loan loss reserves/NPAs	0.00	0.00	1000.63	520.13	314.15	366.98
Leverage (%)						
Total equity/total assets	22.18	19.63	19.84	19.27	16.41	19.47
Total equity and reserves/total loans and MBS	37.89	32.87	31.11	26.87	22.09	30.17
Liquidity (%)						
Total loans and MBS/total assets	58.52	58.38	62.84	70.63	73.22	64.72

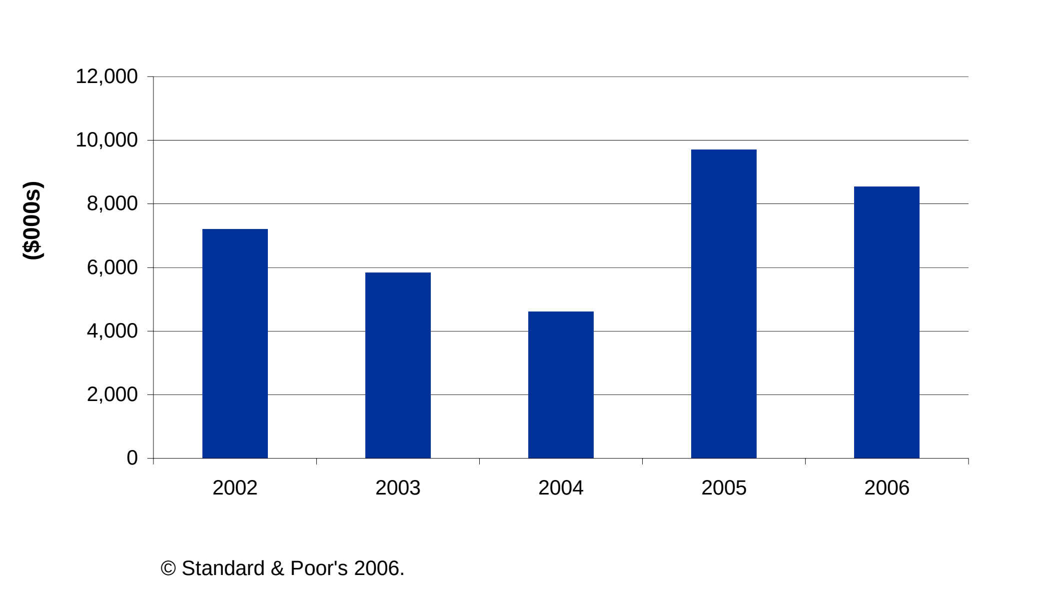
Table 2

Iowa Finance Authority Five-Year Average Financial Ratios (2001-2005)	IFA	All 'AA-' HFAs	All 'AA' HFAs	All 'A+' HFAs	All HFAs
Profitability (%)					
Return on average assets	0.87	0.65	1.07	0.47	0.81
Return on assets before loan loss provision and extraordinary item	0.92	0.76	1.17	0.52	0.90
Net interest margin	1.34	1.25	1.68	0.73	1.33
Asset Quality (%)					
NPAs/total loans and real estate owned	0.03	2.40	2.84	2.95	2.50
Loan loss reserves/total loans	0.32	1.35	2.52	0.90	1.68
Loan loss reserves/NPAs		97.73	94.09	22.35	343.94
Leverage (%)					
Total equity/total assets	21.17	14.27	19.50	9.54	15.46
Total equity and reserves/total loans	34.78	24.23	30.33	15.52	24.93
Liquidity (%)					
Total loans/total assets	61.11	64.00	70.66	66.94	67.16

Table 3

Iowa Finance Authority Trend Analysis	2000	2001	2002	2003	2004	2005	2006
Total assets ($000s)	425,902	449,921	563,855	667,798	684,161	754,715	949,853
% Change		5.64	25.32	18.43	2.45	10.31	25.86
Total debt ($000s)	293,635	315,663	414,019	511,552	522,321	583,944	765,578
% Change		7.50	31.16	23.56	2.11	11.80	31.10
Total equity ($000s)	113,328	112,148	125,046	131,074	135,727	145,435	155,876
% Change		(1.0412)	11.50	4.82	3.55	7.15	7.18
Revenues ($000s)	31,331	34,351	38,556	41,160	46,454	55,826	60,969
% Change		9.64	12.24	6.75	12.86	20.17	9.21
Net income ($000s)	4,990	(225)	7,214	5,836	4,605	9,708	8,531
% Change		(104.5084)	3,106.87	(19.0999)	(21.0965)	110.81	(12.1204)
Total loans and MBS ($000s)	203,393	248,319	329,987	389,849	429,948	533,060	695,508
% Change		22.09	32.89	18.14	10.29	23.98	30.47
Nonperforming assets ($000s)	N.A.	N.A.	N.A.	N.A.	195	426	720
% Change	N.A.	N.A.	N.A.	N.A.	N.A.	117.93	69.01
Loan loss reserves ($000s)	N.A.	N.A.	N.A.	2,911	1,956	2,215	2,261
% Change		N.A.	N.A.	N.A.	(32.8066)	13.24	2.08

Iowa Finance Authority
Net Income



Iowa Finance Authority Total Assets